

**Issue:** Graphic Arts Exemption

2. The Taxpayer was formed from numerous small corporations in 1987.

The Taxpayer is domiciled in .

3. The Taxpayer has seven subsidiaries and twenty-five divisions, each detailed in Department's Exhibit No. 6 (the auditor's workpapers and schedules segregating the sales locations).

4. The Taxpayer makes and sells various personalized and nonpersonalized paper products and accessories. These items consist of wedding invitations and stationery; Christmas cards; commercial stationery; business cards and letterhead stationery and envelopes. (See Department's Exhibit No. 6, auditor's summation of "History and Organization of Business".)

5. The records reviewed in this audit were primarily stored on microfiche, and were poorly maintained for viewing purposes. This situation caused the auditor hardship in accessing resale verifications and debt collection problems.

6. The Taxpayer supplied exemption certificates at the hearing, which were verified for registration in post-hearing procedures. (Taxpayer Exhibit No. 2)

7. Taxpayer's Exhibits No. 1 (a 32-month chronological schedule of the subject audit) and No. 7 (Taxpayer's agreement with Department authorizing a test check/statistical sampling audit for consumable supplies from January 1, 1988, through March 31, 1988) evidence that the auditor's projection for consumable supplies and fixed assets included purchases outside of the test period scope.

8. There is a finding that a bad debt allowance was not made by the auditor.

CONCLUSIONS OF LAW The Retailers' Occupation Tax Act, (Illinois Revised Statutes, Chapter 120, Paragraph 443) provides the following:

"As soon as practical after any return is filed, the Department shall examine such return and shall if necessary correct such return according to its best judgment and information, which return so corrected by the Department shall be prima facie correct and shall be prima facie evidence of the correctness of the amount of tax due as shown herein."

The statute has been strictly construed insofar as establishing a prima facie case is concerned, and the Illinois Courts have universally sustained a prima facie case based upon the corrected tax return. *Fillichio v. Department of Revenue*, 15 Ill.2nd 327 (1985).

Once the corrected return is offered into evidence, there is a statutory burden placed upon the Taxpayer to establish by competent evidence that the corrected return of the Department is incorrect, and until the Taxpayer provides such proof, the corrected return is presumed correct. *Masini v. Department of Revenue*, 60 Ill. App.3rd 11 (First Dist. 1978). In order to overcome the presumption of validity attached to the Department's corrected return, the Taxpayer must produce competent evidence identified with its books and records in showing that the Department's returns are incorrect.

The Taxpayer has produced competent evidence to warrant an adjustment in the tax from XXXXX to XXXXX.

All acceptable exemption certificates proffered in Taxpayer's Exhibit No. 2 have been verified by computer, and have been deleted from the exceptions report.

Pursuant to Taxpayer's Exhibit No. 7, the projection for consumable supplies and fixed assets are concluded to contain purchases from outside of the test period scope, and have been deleted from the exceptions report.

A bad debts allowance is provided for in the Retailers' Occupation Tax Act, and this allowance has been made in the amount of 4%, reflective of the ratio for 1989. This allowance was permitted on net tax due, after all allowances were accounted for.

The auditor relied on 86 Illinois Administrative Code 130.1995, a regulation promulgated under the Retailers' Occupation Tax, in assessing a Retailers' Occupation Tax to personalized Christmas cards. The subject provision reads in pertinent part:

"Section 130.1995 Personalizing Tangible Personal Property

a) When The Tax Applies

1) Thermometers, pencils, pens, mirrors, silverware, notebooks, diaries, baby books, guest registers and other similar books of general utility for the recording of information, brief cases, wallets, toys, paper weights, pins and other jewelry, watches, rulers, match books, playing cards, blotters, calendars, greeting cards, bags and other fairly standard salable containers, napkins, dishes (whether made from paper or some other material), handkerchiefs and other articles of merchandise which bear the name, monogram or trade-mark of the purchaser or of some other person, or which bear advertising inscriptions of the purchaser or of some other person, have intrinsic usefulness and general utility and so have commercial value (i.e., value to persons other than the purchaser), notwithstanding the fact that such items are personalized for the purchaser by the seller by printing, engraving or some other process by means of which the purchaser's name, monogram, trade-mark or special advertising matter is placed upon the article for the purchaser by the seller. (86 Ill. Adm. Code 130.1995(a)(1))"

Although the term "greeting cards" in this section would at first blush logically extend to personalized Christmas cards and thereby subject such sales to ROT, the language here must be read in conjunction with Section 130.2000(B)(2) of the Department's regulations. The pertinent language there reads:

...a person who is engaged in the graphic arts also incurs Retailers' Occupation Tax... of items which he produces on special order if such item serves substantially the same function as stock or standard items of tangible personal property that are sold at retail. Items which "serve substantially the same function" as those which, when produced on special order, could be sold substantially as produced to someone other than the original purchaser at substantially the same price. (Emphasis supplied)

When read together, it becomes evident that the Department does not intend for personalized Christmas cards to be subject to Retailers' Occupation Tax upon their sale, but rather to the Service Occupation Tax. Under the regulatory provision, such cards could not be sold as produced to someone other than the original purchaser at any price other than salvage value, let alone at substantially the same price as originally paid. Personalized cards such as the ones which are the subject of these proceedings have virtually no utility to anyone other than the one for whom they are produced. Accordingly, ROT is inappropriately applied here.

Regarding Taxpayer's Exhibit No. 1, (the 32-month chronological

schedule of the subject audit), it is concluded that no error was committed when the auditor moved the audit period to a current date. While the auditor originally contemplated and initiated a sampling for a two-year audit covering the years 1987 and 1988, in the auditor's discretion, the year 1989 was included in the scope of the audit due to tax law changes taking effect as of January 1, 1990. This would allow the subsequent audit to commence upon current legal procedural changes, which were to affect the Taxpayer prospectively.

It must be noted that the auditor originally used 50% of the gross receipts as the tax base. In the revised assessment, a 37% cost factor was taken on a 100% tax base. The 100% base reflects a cost basis determined after evidentiary materials were proffered at the hearing.

A 5% Service Occupation Tax allowance is recommended on the cost basis; the Taxpayer's contention that the subject allowance be computed on the gross basis is without merit. Service occupation taxes not disclosed on the invoices may not be presumed in the tax base.

The disputed interest calculation is not meritorious; the average interest method is proper agency procedure, and the calculation thereon was accurate.

Specifically, to address the computation of the interest in the adjusted Notice, it must be noted that the Taxpayer made partial payment of \$150,00.00 in February of 1991. Interest of \$57,188.00 is due from the beginning of the audit period, January 1, 1987, through February of 1991. After the recommended tax adjustments were made, \$28,356.84 is due from the Taxpayer beyond the \$150,000.00 paid. (Total tax liability is \$178,357.00). Consequently, additional interest in the amount of \$24,797.00 is due on the remaining liability calculated from January 1, 1987, through November of 1994. These interest figures are consolidated and apportioned on the corrected Notice amongst the six separate tax liabilities computed.

RECOMMENDATION It is my recommendation that Notice of Tax Liability

No. XXXXX be adjusted and finalized as memorialized above.

William J. Hogan  
Administrative Law Judge